sion, and the court below made no effort to resolve the conflict.

The Fifth Circuit's misguided reasoning is well demonstrated by reference to the ultimate conclusion reached, where it said:

> "In final analysis, *putting to one side the issue of congressional intent,* the petitioner's challenge to the FPC order addresses itself to the competency of the Commission to choose between competing accounting theories and competing economic guesses. We see nothing irrational in the Commission's choice." (359 F. 2d at 339) (emphasis supplied)

It is difficult to imagine how the issue of Congressional intent can be put to one side and a correct decision reached. Petitioner's whole case devolved upon the question of Congressional intent in making the tax benefits of liberalized depreciation available to Petitioner and other pipelines. By side-stepping this critical point, there is, in truth, no decision at all on the real issue raised by Petitioner's appeal. In *Panhandle,* the Court of Appeals for the District of Columbia explicitly held that the Commission's order there was "consistent with the Congressional policy underlying the tax statute" (*Id.* at 663). By no stretch of the imagination can *Panhandle* stand side by side with the Fifth Circuit's decision, as it reaches a diametrically opposite result.

The conflicting decisions reached by the two appellate courts illustrate the problem with which the regulated companies have been faced over the last twelve years since the enactment of Section 167 of the Internal Revenue Code of 1954. It is time, *amicus* submits, that the issue herein and the conflicting decisions thereon be resolved by this Court.

2. The Decision of the Court Below Raises an Important Question Which Should Be Resolved by This Court

In ruling that the Commission's treatment of liberalized depreciation was within the Commission's regulatory competence and hence should be permitted to stand, the court below, in sharp contrast to the District of Columbia Court of Appeals in the *Panhandle* case, ignored the clear intent of Congress and has permitted an improper substitution of Commission judgment for that of Congress in a matter of vast national importance.

Congress, in 1954, enacted Section 167 as an investment incentive for the business community generally, making no distinction between regulated and non-regulated industries. The stated Congressional purpose in making these liberalized depreciation methods available was to stimulate all segments of the economy by accelerating the placement of funds in the hands of all businesses as an inducement to new investment. As stated by the House Ways and Means Committee (H. Rep. No. 1337, 83d Cong., 2d Sess., p. 24):

> ". . . For *all* segments of the American economy, liberalized depreciation policies should assist modernization and expansion of industrial capacity, with resulting economic growth, increased production, and a higher standard of of living."[2] (emphasis supplied)

The choice of the means to the end of aiding the national economy was entirely deliberate; it was only after a spirited debate that monetary relief was granted by Congress to businesses generally in Section 167 rather than to individuals in the form of income

[2] To the same effect, see also the Report of the Senate Finance Committee (S. Rep. No. 1662, 83d Cong., 2d Sess., p. 25).

tax reductions.[3] Liberalized depreciation, moreover, was viewed by its supporters as a tax deferral, a shift in deductions between taxable years, rather than an outright loss in revenue. Perhaps even more significant, the measure was expected to have such a substantial incentive effect that, even in the early years, there would be no loss in revenues.[4]

The optional aspect of liberalized depreciation deserves particular emphasis. For if a company does not elect to take liberalized depreciation, there can be no benefits to anyone, whether denominated a "tax saving", as the Commission found, or a tax deferral, as stated by Congress.

Uncertain whether to elect to take accelerated depreciation on their new assets, many gas pipeline companies sought an early determination from the Commission of the regulatory treatment to be accorded this incentive measure. On June 30, 1956, after a full hearing, the Commission made such a ruling[5] in which it specifically held that the Congressional purpose in enacting Section 167 required that the gas pipelines depreciating assets under this section be permitted to retain and realize the benefits of liberalized depreciation.[6]

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[3] H. Rep. No. 1337, *supra*, at App. B4, where the Committee minority states that the most effective incentive to business would be to increase consumer purchasing power by tax reductions to individuals. This viewpoint found expression in proposed amendments in both the Senate and the House to increase the personal income tax exemption. For a comprehensive analysis dealing with this and other aspects of this legislation, see *Liberalized Depreciation; About-Face by the FPC*, 30 Va. L. Rev. 298-366, March 1964.

[4] H. Rep. No. 1337, *supra*, at p. 25.

[5] *Amere Gas Utilities Co., et al.*, 15 FPC 760, 781 (1956).

[6] *Id.* at 782.

Following *Amere*, the Commission, from that time until the instant case, uniformly permitted normalization.[7] Pipeline companies, relying on these formal Commission pronouncements, elected to take advantage of the tax incentives urged upon them by Congress. Moreover, the Commission's treatment of tax deferrals for rate case purposes received judicial approval in every instance where the Commission's action was reviewed, including the Fifth Circuit in *El Paso Natural Gas Co.* v. *FPC*, 281 F. 2d 567 (1960), *cert. den.* 366 U.S. 912; see also *Cities of Lexington, et al.* v. *FPC*, 295 F. 2d 109 (4th Cir. 1961), and *Panhandle Eastern Pipe Line Co.* v. *FPC*, 316 F. 2d 659 (D.C. Cir. 1963), *cert. den.*, 375 U.S. 881. The Commission decision under review is, therefore, a complete "about-face."

Nor is this complete reversal applicable *in futuro* only. The Commission's order directs that accumulated deferred taxes relating to *past* plant additions be deducted from the rate base, thus denying any return upon the tax deferrals already accrued. The pipelines, acting in good faith reliance upon the Commission's judicially-sanctioned formal pronouncements, initially elected, and continued to utilize, liberalized depreciation and irrevocably committed the funds so generated for the construction of new facilities and the expansion of their plants. For so doing, they are now being

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[7] *E. g., El Paso Natural Gas Company*, 22 FPC 260; *United Fuel Gas Co.*, 23 FPC 127; *Phillips Petroleum Co.*, 24 FPC 537; *Northern Natural Gas Co.*, 25 FPC 431; *Kansas Nebraska Natural Gas Co.*, 25 FPC 448; *Panhandle Eastern Pipe Line Co.*, 25 FPC 550. This was consistent with the Commission's judicially-sanctioned treatment of Section 168 of the Internal Revenue Code which permitted rapid depreciation of emergency facilities constructed in the interest of national defense. *City of Detroit* v. *FPC*, 230 F. 2d 810, 822 (D.C. Cir. 1955), *cert. den.*, 352 U.S. 829.

penalized, not only prospectively, but retroactively. Indeed, had the companies known what the Commission's action here would be when the question was first raised in *Amere* almost twelve years ago, they would not have elected to use liberalized depreciation. Absent the advantages of the deferred tax funds which normalization would generate, straight-line depreciation is the only stable, suitable, consistent method for the regulated companies to use in computing tax depreciation deductions.

The error in the affirmance by the court below of the Commission's 180-degree turn in this case lay principally in its refusal to recognize the specific Congressional intent embodied in the tax statute and in its inability to reconcile the rate provisions of the Natural Gas Act with what it thought were conflicting provisions of Section 167 of the Internal Revenue Code of 1954. In essence, the court found that the aims and objectives of Section 167, in providing tax benefits to the taxpayer (*i.e.*, the pipeline) were incompatible with the aims and objectives of Sections 4 and 5 of the Natural Gas Act which require that only just and reasonable rates be charged, citing *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944). The short answer is that there is no incompatibility whatever between the two statutes as is evident from the long list of decisions (cited above, p. 9) in which Federal appellate courts have considered this question. While it is true that the *Hope* case, as the court below points out, is often cited for the proposition that the primary purpose of the Natural Gas Act of 1938 was to protect the consumers, it is also true that the Supreme Court, in that case, recognized that "The rate-making process under the Act, i.e., the fixing of 'just and reasonable' rates, involves a balancing of the investor and the con-

sumer interests" (*Id.* at 603). No one denies, on the other hand, that Section 167 was enacted for the primary benefit of the taxpayer. Thus, it can be seen that the two statutes are designed to serve separate and distinct purposes. The Court of Appeals for the District of Columbia in the *Panhandle* case, *supra,* had no difficulty in reconciling the separate statutory purposes in approving normalization coupled with a return of 1½ percent on the funds generated thereby:

> "Here the Commission, following its decision in Northern Natural Gas Co., 25 F.P.C. 431 (1961), 'divided the benefits of liberalized depreciation between the regulated company and the rate-payer' giving the 'major portion of the benefits to the rate-payer.' It permitted Panhandle 'only so much of [a return on funds generated by the use of liberalized depreciation] as is necessary to provide it with a sufficient incentive to continue to use liberalized depreciation.' Thus, a substantially lower rate of return was attributed to those funds than to other capital." 316 F. 2d at 661.

Crucial to the Commission's new position is its finding that the intent of Congress to stimulate the economy will be fulfilled by flowing through the benefits of liberalized depreciation to the consumers in the form of lower rates thereby increasing consumer buying power which, in turn, will increase the demand for natural gas with a consequent need for more facilities. But had Congress intended that kind of stimulus, it would have so provided. Congress did not simply express a desire to stimulate the economy by enactment of Section 167. It also chose a specific method to do so—by provision of tax deferred funds to business for investment. The legislative history of Section 167, discussed *supra* (pp. 7-8), shows that efforts to stimulate the economy by tax reductions were ex-

pressly rejected by the Congress in favor of the tax incentives for industry provided by Section 167. The Commission's reasoning here is identical with that of the minority views in Congress which opposed Section 167. The Commission is thus adopting the method that Congress itself rejected.

In addition, the record in the instant proceeding is barren of any factual evidence to support such a finding. Had an opportunity been provided as sought by both Petitioner and the pipelines, it would have been shown that a reduction in rates, of the magnitude here involved, would not provide the stimulus contemplated by the Commission.

Accepting the Commission's reasoning, the Court of Appeals concluded that a regulated utility will *never* be required to pay higher income taxes, because of its election to claim liberalized depreciation, *unless* its gross plant declines in dollar value as a result of lower demand or lower plant construction cost (359 F. 2d at 336). Both the court and the Commission conceded that this conclusion rested on speculation as to what the future risks of the gas companies would be both in terms of growth potential and in having the cash requirements in the future to pay the deferred taxes. Though the record on this important question is devoid of meaningful, substantial evidence, as to the accuracy of its premises, the court, with the same illogic pervading the Commission's order, concluded that the case for normalization requires more speculation than the case for flow-through. Quite aside from the fact that many of the Commission's contentions were presented to Congress and rejected, normalization requires far less speculation than flow-through. This is so because normalization provides no higher rates to consumers than would be charged if the pipe-

lines did not utilize liberalized depreciation for tax purposes. The risks of economic obsolescence and competition present a far greater danger under flow-through than under normalization. Flow-through places an intolerable burden on the pipeline companies to assume the risk of not having sufficient revenues in the future to pay the higher taxes resulting from present use of liberalized depreciation. Moreover, flow-through, in contrast to normalization, distorts the true earnings picture of individual pipeline companies, making this important test of investor interest and reliance meaningless, if not completely misleading. Such a result runs counter to the clear responsibility which the Commission has to the investing public with respect to the earnings reported by industries subject to its regulation.

3. The Commission Procedure Denied a Fair Hearing

It is indeed "singularly eccentric", as concluded by the court below, "that a matter as important to the natural gas industry as the Commission's about-face on liberalized depreciation should be resolved" (359 F. 2d at 341) in long pending rate cases of one of the smallest interstate gas pipeline companies. The court below erred, however, in holding that such admitted eccentricities do not render the procedure below fatally defective.

Even assuming, *arguendo*, that the Commission properly extended the scope of Alabama-Tennessee's rate case to include the liberalized depreciation issue, the procedure adopted by the Commission effectively denied to INGAA and other interested parties, as well as Alabama-Tennessee, their statutory right to participate fully in the hearing; to submit evidence; to produce and cross-examine witnesses; and to spread upon

the record all pertinent facts bearing upon this issue of industry-wide importance. *Morgan* v. *United States,* 304 U.S. 1, 18-19 (1938); *Ohio Bell Telephone Company* v. *PUC,* 301 U.S. 292, 304 (1937). Instead of affording such procedural and substantive safeguards before adopting the "about-face" order which eventuated, the Commission at the very last stage of the rate proceeding, and 20 months after the hearing record was closed, invited participation, as *amici,* "either in the oral argument, or by the filing of written briefs", by any person, company, association or governmental authority "having an interest in the problem" (R. 64-66).

Nor did the Commission permit those "having an interest in the problem" to develop an evidentiary record even though it conceded, in its Opinion, that the tax consequences of liberalized depreciation must be evaluated in the light of such factual considerations as demand for gas, plant capacity, adequacy of gas reserves, level of plant construction costs and the likelihood and impact of declining plant additions (R. 142). To resolve these factual matters, the Commission relied on statistical data outside the record on the ground that they were subject to administrative notice. However, not only do these critical underlying issues involve highly controversial factual matters, but cross-examination would have shown the material on which the Commission relied to be either unreliable or inapplicable. The Commission's action thus improperly utilized the doctrine of administrative notice as "a pretext for dispensing with a trial" at which the interested parties would have been afforded an opportunity

to offer evidence and cross-examine on these critical factual issues. Cf. *Ohio Bell Telephone Co.* v. *PUC*, *supra*, at 302.

Objections to the procedure followed by the Commission were shrugged off with the comment that other pipelines would be afforded an opportunity (after the fact) to show cause why the determination made here is not applicable to them (R. 127). With *scant* opportunity in the first and precedent-setting case to show why the Commission should not reverse its earlier judicially-approved decisions requiring normalization and *no* opportunity to establish evidentiary support for their position, the burden was imposed upon the pipelines to show cause, in the form of exceptional circumstances why they should continue to receive the tax incentives which Congress specifically made available to them. It is a hollow gesture to assert, as does the Commission and the court below, 359 F. 2d 343, that each pipeline company will be given the opportunity to show why it should be permitted to follow normalization when employing liberalized depreciation. As this Court stated in somewhat comparable circumstances, to place that burden on these companies "is in effect to make its hearing a rehearing . . . rather than a hearing on the merits of its own application." Such a hearing does not satisfy either the "spirit or intent" of the law. *Ashbacker Radio Corp.* v. *FCC*, 326 U.S. 327, 331 (1945).

CONCLUSION

For these reasons, as well as those stated by Petitioner, Alabama-Tennessee, the petition for a writ of

certiorari, filed herein by Alabama-Tennessee, should be granted.

Respectfully submitted,

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